



An Analysis of the Banking Industry using Porter’s Five Forces Model

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Abstract

The banking industry has been influenced by opposing philosophies from its inception, such as the desire for greater financial stability through government intervention or economic freedom through minimizing the power of the government. This research paper attempts to synthesize the extant literature on key factors for success in banking.

I conducted a literature review, based on the secondary data collected from major business databases such as ABI/Inform, OneFile, and JSTOR. Of the 56,413 peer-reviewed articles identified as relevant to ‘banking industry,’ 44 articles used Michael Porter’s Five Forces Model and 10 were selected based on relevance and examined in detail.

Findings of the current research indicated that there is no “one size fits all” solution that foster future growth and performance of the banking industry. Changes to the industry’s internal and external culture are necessary. Some examples include: Improvement through the use of technology and analytics, modernization of customer engagement, and renewal of efficient operations through optimization of the banking current structure. Agility and continuous innovations are necessary to seize the opportunity to provide customers with a new service and create a next-generation customer experiences. To proactively capture the emerging opportunities in the industry banks must also embrace new technologies, channels, and strategies to succeed in this new era.

The current research provides value to the current and future banking professionals in understanding the ‘big picture’ of the industry and importance of developing strategies to enhance the performance of the organization.

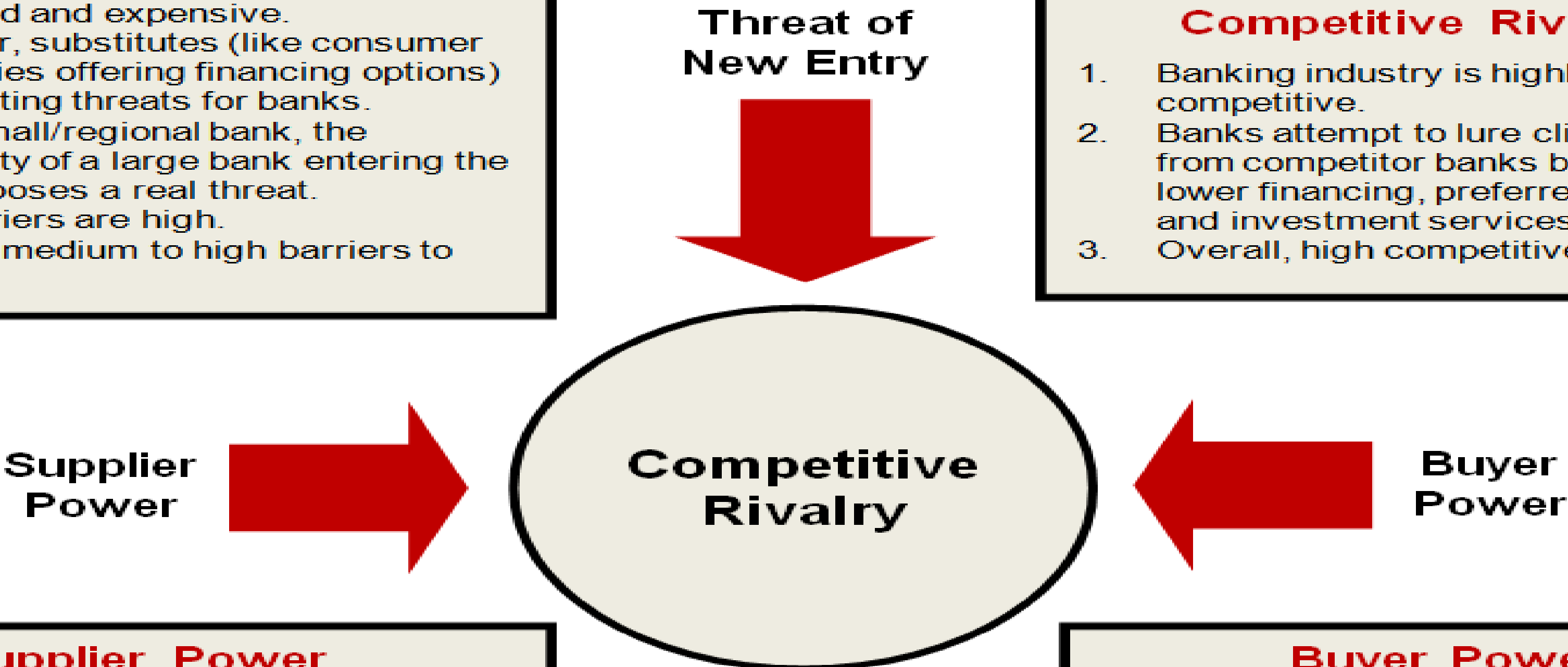
Porter’s Five Forces

Threat of New Entry

1. Entering the banking industry is regulated and expensive.
2. However, substitutes (like consumer companies offering financing options) are creating threats for banks.
3. For a small/regional bank, the possibility of a large bank entering the market poses a real threat.
4. Exit barriers are high.
5. Overall, medium to high barriers to entry.

Competitive Rivalry

1. Banking industry is highly competitive.
2. Banks attempt to lure clients away from competitor banks by offering lower financing, preferred rates and investment services.
3. Overall, high competitive rivalry.



Supplier Power

1. There is only one big supplier – the central bank (RBI), or the bank of banks. The RBI has total control over the banking industry. A little change in interest by the RBI can have tremendous effect on the whole industry.
2. If employees are also considered suppliers (of their human capital/services), then the bargaining power is low at the lower end (clerks, tellers etc.), and high at the higher end (top management).
3. Overall, high supplier power.

Buyer Power

1. Doesn’t seem big on the face of it as a customer can switch to any bank anytime.
2. Switching costs are however high. If a person has a mortgage, car loan, credit card, savings account and mutual funds with one particular bank, it can be extremely tough for that person to switch to another bank. So most people would still rather stick with their banks for years.
3. On the other hand, large corporate clients have high bargaining power, as they provide big business to banks and are also more profitable than retail customers.
4. Overall, buyers have low to medium bargaining power.

Threat of Substitution

1. Plenty of substitutes have emerged in the banking industry.
2. Whether it is insurance, mutual funds or fixed income securities, chances are there is a non-banking financial services company (NBFC) that can offer similar services.
3. On the lending side of the business, banks are seeing competition rise from unconventional companies. Electronics and automobiles, for instance, offer preferred financing to customers who buy big ticket items.
4. Overall, rising threat of substitutes.

Conclusion

To sustain a competitive advantage requires:

- Bold ambidexterity strategies that extend deeper into consumers’ lives and their daily interactions .
- Identify the needs of their tech-savvy millennial customers through improved customer engagement and consumer experience.
- Gain a better understanding of consumer purchases and their distribution channels.
- Implement growth strategies outside of its core existence through the use of technology.
- Major internal change of the mindset and talent of their employees.
- Renewal of efficient operations by providing customers with value and service at a cost (that allows banks to be competitive while generating an acceptable return)